MAR 27 1973

No. 72-1308

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1972

Norman Shutler and Virginia Shutler; and,
A. H. Turner and Edith Turner, Petitioner,

vs.

United States of America. Respondent.

PETITION FOR WRIT OF CERTIORARI

To the United States Court of Appeals for the Tenth Circuit

Norman Shutler, Attorney
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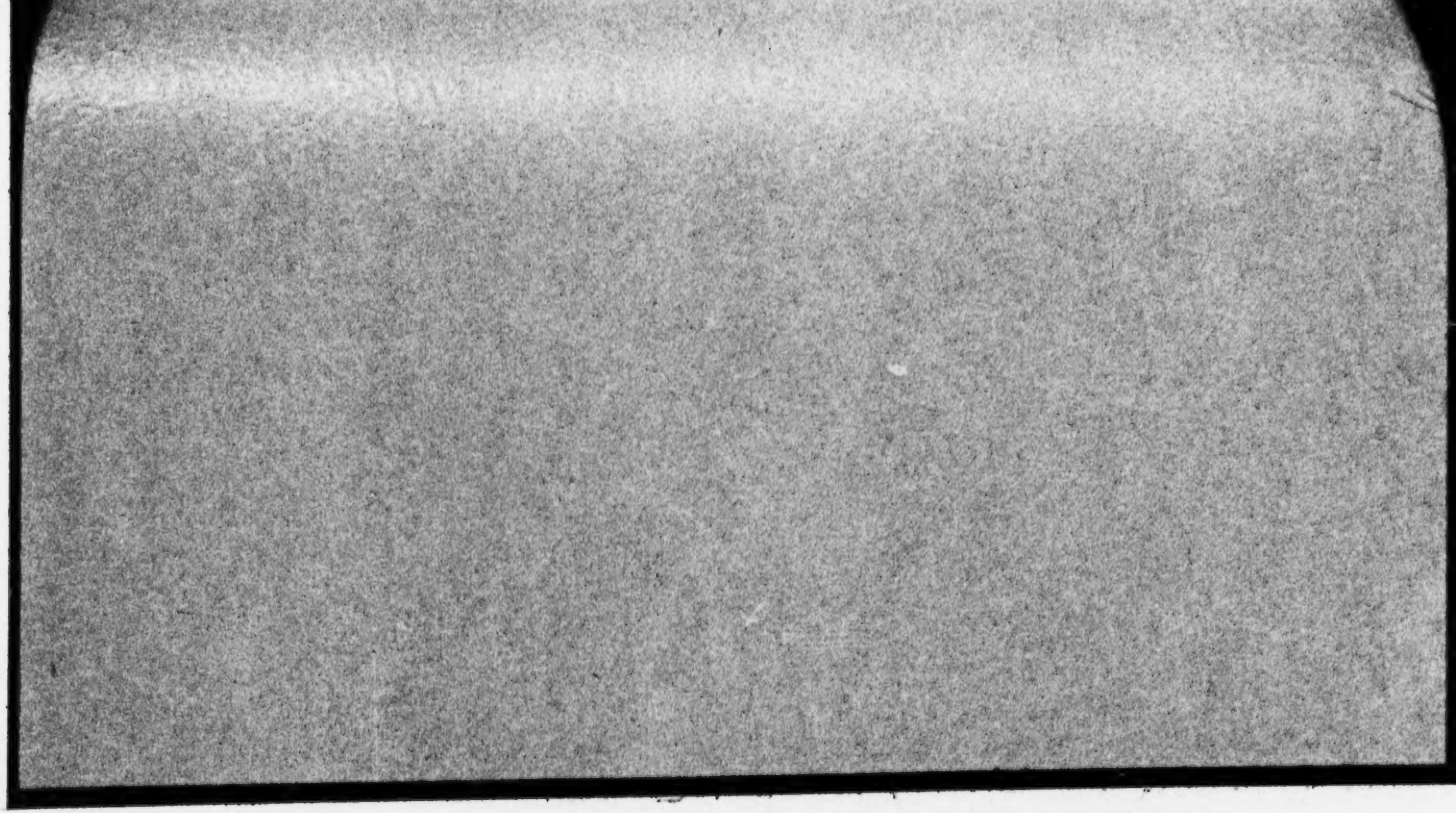
March, 1973.



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IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1972

No.....

Norman Shutler and Virginia Shutler; and,
A. H. Turner and Edith Turner, Petitioners

vs.

United States of America, Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

Norman Shutler and Virginia Shutler; and A. H. Turner and Edith Turner, the petitioners herein, pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Tenth Circuit entered in the above entitled case on December 29, 1973. Rehearing denied January 22, 1973.

OPINIONS BELOW

The opinion and judgment of the Circuit Court of Appeals for the Tenth Circuit is unreported and is printed in Exhibit A hereto, infra, page 9. The Journal Entry of Judgment of the United States Court for the Western District of Oklahoma is printed in Exhibit A hereto, infra, page 23.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 29, 1972 (infra, Exhibit A, page 9). Rehearing was denied on January 22, 1973 (infra, Exhibit A, page 28). The jurisdiction of the Court is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

Whether the petitioners were entitled to deduct from their gross income for the year 1966 the proportionate amount expended for the cost of acquiring a Preference Right Agricultural Lease covering 160 acres of land owned by the State of Oklahoma.

STATUTE INVOLVED

Treasury Regulations on Income Tax (1954 Code) Section 1.162-11 provides, as follows:

"(a) ACQUISITION OF A LEASEHOLD. If a leasehold is acquired for business purposes for a specified sum, **the purchaser may take a deduction in his return an aliquot part of such each year based on the number of years the lease has to run** . . . . See Section 178 and the regulation thereunder for **rules governing the effect to be given renewal options** in amortizing the costs incurred after July 28, 1958, of acquiring a lease." (Emphasis ours.)

STATEMENT

This is an action wherein the taxpayers acquired in 1966 a School Land Lease on quarter section of land in Kingfisher County from the Commissioners of the Land Office of the State of Oklahoma. The successful bid for the acquisition of this lease was $15,000.00, of which $2,000.00 was allocated to the improvements and $13,000.00 allocated to the cost of acquiring the lease. The high bid and acquisition of the lease was subject to a relinquishment of the lease in favor of the taxpayers and approval by the Commissioners of the Land Office of the taxpayers as new tenants, all of which was accomplished, approval was made and on August 23, 1966, the taxpayers obtained from the Commissioners of the Land Office of the State of Oklahoma a lease on the quarter section for the remainder of the five-year term expiring December 31, 1966. Subsequently, in 1967 taxpayers were successful in renewing the lease with the Commissioners of the Land Office for a five-

year term. Taxpayers filed timely returns for the year 1966, claiming as a deduction the cost of acquiring the Preference Lease which expired as of December 31, 1966. Subsequently, the returns were audited, the deduction disallowed by the government and the taxpayers then paid the tax, filed claims for refund, which were disallowed. Then the taxpayers filed an action in District Court where their claim was allowed. This judgment of the District Court was appealed by the government to the United States Court of Appeals of the Tenth Circuit, where the action of the District Court was reversed and petition for rehearing was denied on January 22, 1973, resulting in the filing of the within Petition for Certiorari.

ARGUMENT

It is respectfully submitted that the Court of Appeals, in its opinion of December 29, 1972, has rendered the "Rule of Law" subservient to custom and usage, thereby opening a Pandora's box insofar as the stability of the law of real property is concerned in general and the applicability of the tax regulations to the law of real property in particular.

Taxpayers have no real quarrel with Nachman v. Commissioners of Internal Revenue, 191 F. 2d 934 (5th Cir. 1951), as cited by the Court of Appeals in its opinion of December 29th, insofar as the Nachman case announces a rule applicable to the renewal of liquor licenses, nor do

we quarrel with analogous cases to Nachman dealing with acquisition of television and radio licenses; however, these cases do not deal with the acquisition of a leasehold estate and therefore do not fall under Treasury Regulation on Income Tax (1954 Code), Section 1.162-11, which provides, as follows:

> "(a) ACQUISITION OF A LEASEHOLD. If a leasehold is acquired for business purposes for a specified sum, **the purchaser may take a deduction in his return on aliquot part of such each year based on the number of years the lease has to run** . . . . See Section 178 and the regulation thereunder for **rules governing the effect to be given renewal options** in amortizing the costs incurred after July 28, 1958, of acquiring a lease." (Emphasis ours.)

In the present case, we are dealing with a leasehold situation that falls specifically under Section 1.162-11, whereas, Nachman, Supra, and the other cases cited by the Court of Appeals and the government as set forth in the Court of Appeals' opinion in this case deal with tax situations which do not deal with leasehold situations. Therefore, it is submitted that the Court of Appeals' opinion in this case was based on non-analogous authority. Under the applicable Treasury Regulation, since the lease in question expired in the year in which it was obtained, the entire cost was deductible that year.

The government takes the position that since it was customary for the Commissioners of the Land Office to renew leases, we have a lease for an indefinite period. There is no question but that the custom of the Commissioners of the Land Office is to, in fact, renew leases; however, Rules and Regulations of the Commissioners of the Land Office provide, at Paragraph 4107, as follows:

> "The term 'Preference Right Lease' means the right of a lessee to purchase the land he is leasing at the highest bid, if the Commissioners elect to sell said leased land during the term of his lease. . . . **and has no meaning or application entitling lessee to a right to re-lease at the end of his term.**" (Emphasis ours.)

There is clearly no **right** of renewal, only a custom. The significance of the preeminence of the rule of law over custom has been dealth with by the Court of Appeals in Scully v. United States, 409 F. 2d 1061, (10th Cir. 1969), a condemnation suit, albeit not tax case, where the question arose as to the division of funds resulting from a taking in condemnation as between landlord and tenant. In Scully, the lessee maintained that he had an annual lease from Scully and since the practice of Scully was to routinely extend or renew agricultural land leases which did not contain renewal provisions that the lease could be properly interpreted to be longer than one year for the purpose of determining division between lessor and lessee of the

amount paid by the condemnor, this being especially true since the lessee had occupied the land for nearly thirty years. In Scully, the Court, at page 1065, puts the custom aspect in its proper prospective when it states:

> ". . . It is one thing to rely upon custom and usage to clarify incidental problems of lease interpretation, but it is quite another to extend the term or duration of the tenancy through such dubious means. . ."

This is precisely the point we now urge. The government's contention is that the lease is, in effect, extended by custom so as to take the lease outside of the taxpayers' contention. The government maintains that the custom of renewal of the lease enhances the value of the lease. With this, we have no quarrel. The lessee in Scully maintained that Scully's practice of renewing leases enhanced the value of the leasehold. In Scully, the Court of Appeals stated, citing with approval from other cases:

> ". . . 'Changeable intentions are not an interest in land, and although no doubt such intentions may have added practically to the value of the petitioners' holding, they could not be taken into account****. They added nothing to the tenants' legal rights, and legal rights are all that must be paid for. Even if such intentions added to the saleable value of the lease, **the addition would represent a speculation on chance not a legal right.**' We conclude that the lessee of a one year term is not entitled to recover the market value added by a mere expectation that the lease will be renewed." (Emphasis ours.)

Therefore, in Scully, the Court of Appeals reversed the District Court of Kansas for the reasons above mentioned. We have been unable to find any rulings by this Honorable Court which are precisely in point. However, the decision of the District Court in the present action is completely consistent with the Tenth Circuit's prior decisions in Scully and is further completely consistent with the governing Treasury Regulations.

CONCLUSION

In conclusion, it is respectfully submitted that the ruling of the Court of Appeals handed down on December 29, 1972, is in error in that it fails to give credence to the applicable Treasury Regulation and, therefore, applied inapplicable law to the fact situation herein presented. We respectfully submit that the regulations and cases referred to here are clear and applicable; that the taxpayers are entitled to an order granting certiorari and upon the granting are entitled to the deduction that they claimed on their original returns. The decision of the District Court is correct and based upon the prior decisions of the Tenth Circuit and the applicable Treasury Regulations and should be affirmed.

Respectfully submitted,

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EXHIBIT A

UNITED STATES COURT OF APPEALS

TENTH CIRCUIT

NOVEMBER TERM — 1972

NO. 71-1496

NORMAN SHUTLER and VIRGINIA SHUTLER,

Plaintiffs-Appellees,

v.

UNITED STATES OF AMERICA,
Defendant-Appellant.

A. H. TURNER and EDITH TURNER,

Plaintiffs-Appellees,

v.

UNITED STATES OF AMERICA,
Defendant-Appellant.

Appeal from the United States District Court

For the Western District of Oklahoma
(D.C. Nos. Civ. 71-10 and Civ. 71-11)

Thomas E. Baker, for Plaintiffs-Appellees.
Leonard J. Henzke, Attorney, Tax Division, Department of Justice (Fred B. Ugast, Acting Assistant Attorney General; Meyer Rothwacks, Bennet N. Hollander and Jane M. Edmisten, Attorneys, Tax Division, Department of Justice; and William R. Burkett, United States Attorney, on the brief), for Defendant-Appellant.

Before LEWIS, Chief Judge, HOLLOWAY and McWILLIAMS, Circuit Judges.

McWILLIAMS, Circuit Judge. (Reassigned for opinion to McWilliams, Circuit Judge, from Holloway, Circuit Judge, on November 16, 1972.)

Norman and Virginia Shutler brought an action in the District Court for the Western District of Oklahoma for refund of income taxes paid for the year 1966. A. H. and Edith Turner at the same time filed a separate proceeding in that same court which also sought a refund of income taxes paid for that same year. These two proceedings were consolidated for purposes of discovery and trial by appropriate order of the trial court and these consolidated cases were then later submitted to the trial court on a comprehensive stipulation agreed to by the parties. Based on the stipulation the trial court made certain findings and

entered judgment against the United States for the Shutlers in the amount of $5,180.50, plus interest, and in favor of the Turners in the amount of $1,046.45, plus interest. The United States now appeals.

As indicated, the essential facts are agreed to by the parties. Virginia Shutler and Edith Turner are parties to the proceeding simply because they filed joint income tax returns for the tax year 1966 with their respective spouses. Norman Shutler and A. H. Turner, hereinafter referred to as the taxpayers, are described in the stipulation as "cotenants in farming operations in Kingfisher County, Oklahoma," and as such they jointly owned or leased various tracts of land used in their farming operation.

The particular tract of land which precipitates this controversy is the northeast quarter of section 36, township 17 north, range 6 west, Kingfisher County, Oklahoma. On April 29, 1966, the taxpayers were high bidders for and purchased the northwest quarter of that section from the Adele Nieman estate. For a number of years prior to 1966 Adele Nieman had been the lessee of the northeast quarter of section 36 under a so-called Preference Right Lease with the State of Oklahoma. This lease covered land owned by the State of Oklahoma and supervised by the Commissioners of the Land Office for that state. On April 29, 1966, the taxpayers also purchased at auction from the Nieman es-

tate the Preference Right Lease to the aforesaid northeast quarter of the section with which we are here concerned. The taxpayers paid a total sum of $15,000 for the lease in question, $13,000 of which was allocated to the cost of acquisition and $2,000 to the value of the improvements thereon. Under the lease the annual rental paid the State for the property was $850.

Pursuant to the requirements of the Land Office of the State of Oklahoma, the Nieman estate executed a relinquishment in favor of the taxpayers. The latter then made formal application for the lease and eventually obtained a lease for the period of time from August 23, 1966, to and including December 31, 1966, from the State. Such period of time incidentally was the balance of time remaining on the five-year lease held by Adele Nieman at the date of her death. Thereafter, the taxpayers obtained a renewal of the lease from the State for a five-year period, i.e., from January 1, 1967, to and including December 31, 1971, at an annual rental of $850. The critical issue in the case relates to the nature of the $13,000 expenditure incurred by the taxpayers in acquiring the lease from the Nieman estate, which in turn concerns the nature of the so-called Preference Right Lease thus acquired by the taxpayers. A bit of background will perhaps place the matter in focus.

The State of Oklahoma, through the Commissioners of

the State Land Office, is entrusted with the leasing and sale of school lands. Such land is owned by the State and the income therefrom is designated for specific purposes. Although some acreage in the past has been sold outright, today practically none is sold, but is leased. Thus the Land Office enters into approximately 3,500 agricultural and grazing leases on these school lands, all for a term of five years, all of which come due on the same date. Approximately half of these leases are so-called Preference Right Leases, under which the State grants the lessee the preferential right to purchase the land he is leasing from the State for an amount equal to the highest bid at an auction sale, if and when the State ever decides to sell.

Prior to 1946, all Preference Right Leases also contained a provision that the lessee had the right to re-lease the land upon the expiration of the lease then in force. This provision was dropped in 1946. However, ever since that date it has been, and is, the policy of the Land Office to re-lease the school lands at the end of the five-year period to, and only to, the person in possession at the expiration of the lease, except for cause, such as, for example, nonpayment of rent, abuse of the land, and the like.

As for the transferring of a Preference Right Lease, the Land Office has the lessee execute a relinquishment in favor of the proposed new lessee. Then following an investigation of the proposed lessee, a new lease is entered

into for the remaining portion of the five-year term of the original lease.

In this general setting, the taxpayers filed their 1966 tax returns with each claiming that he was entitled to deduct from his gross income his proportionate share of the cost of acquiring the Preference Right Lease on the aforesaid northeast quarter of section 36. The Internal Revenue Service disallowed this deduction with the taxpayers paying the full tax and then suing for a refund. As above stated, the trial court ruled in favor of the taxpayers and the Government appeals.

The findings of the trial court are rather meager and give little insight into its reasoning. However, there was the obvious finding that the taxpayers acquired a lease on certain lands in the State of Oklahoma and paid therefor $13,000, which sum was paid during the year 1966 for a lease which expired December 31, 1966. In connection therewith the trial court then went on to make what it obviously believed to be a critical finding to the effect that the lease thus acquired "contained no option, and there was no reasonable certainty that the Commissioners of the Land Office would renew said lease for any given period of time." In this latter regard, the trial court opined that such leases are subject to the "whims of the Oklahoma Legislature, which meets every year and which has over

the years enacted and repealed various laws dealing with the administration of State Lands."

In our view, the trial court's finding that there was no "reasonable certainty" that the Land Office would renew the lease thus acquired by the taxpayers for any period of time is contrary to the stipulation. While it is true that the Preference Right Lease did not itself grant the lessee a preferential right to re-lease at the end of a leasehold period, the fact remains that from the record one can only conclude that it was the unvarying practice to so do. Some proof of this practice, though of course not controlling, is the fact that the taxpayers did in fact obtain a renewal of the lease which they acquired from the Nieman estate.

Concerning the practice of renewing the lease to the party holding it when the lease period expires, the deposition of N. A. Gibson, Chief Counsel for the Commissioners of the Land Office of the State of Oklahoma, was before the trial court as a part of the stipulation, and his declaration, which stands unrefuted, was as follows:

> "Since my association with the department in 1952, it has been the consistent policy of the Commissioner, at the expiration of the term of the lease, to offer a new lease for the ensuing term to the lessee, whether he be a preference right lessee or a non-preference right, lessee, assuming that he has paid his rent, and he has taken proper care of the land."

This policy incidentally was in accord with the Rules and Regulations of the Land Office. Section 4.205 of those regulations provides as follows:

> "Except when specifically ordered by the Commissioners leases will not be offered for bid. Generally, only the owners and holders of expiring leases as reflected by the records of the Commissioners will be entitled to receive new lease forms for execution."

And to the same effect is Section 4.206, which reads:

> "If the holder of an expiring lease, his administrator, executor, heirs and/or devisees do not desire a new lease at the expiration of an existing lease, or a lease has been forfeited or canceled, the Commissioner may order the sale of such lease to the highest and best bidder * * *."

Accordingly, we conclude that the trial court's finding that there was no reasonable certainty that the Land Board would renew the taxpayers' lease when it expired on December 31, 1966, is clearly erroneous. Indeed, in our view the record shows the exact opposite. And the fact that the taxpayers as the holders of the lease when it expired on December 31, 1966, were with reasonable certainty assured of a renewal of their lease is of much legal significance in the resolution of this controversy. In this regard the rule is quite clear that in determining the character of any transaction or arrangement for taxpayers, it is the substance, rather than the form, that controls and that under this principle the terms of a lease may even be disregard-

ed. Highland Hills Swimming Club, Inc. v. Wiseman, 272 F.2d 176 (10th Cir. 1959). See also Babcock v. Phillips, 372 F.2d 240 (10th Cir. 1967).

The taxpayers' basic position, which apparently was adopted by the trial court, is that "since the cost of acquiring the lease in question expired in the year in which it was obtained, the entire cost was deductible that year." In thus arguing, counsel stresses the fact that the taxpayers had no contractual right to renew the lease upon its expiration. As indicated, such in our view ignores the fact that it was nonetheless the practice to renew, which of course explains why the taxpayers were willing to pay the estate of Adele Nieman the sum of $13,000 for a lease which had approximately four months to run and called for an annual rental of only $850. In other words, it is inconceivable that the taxpayers would pay the sum of $13,000 for a lease which had only four months to run, and the $13,000 obviously represented the value of the renewal privilege which by custom attached to the lease.

It is the Government's position that the cost of acquisition of the lease was not an ordinary and necessary business expense, but a capital expenditure. It is the further position of the Government that because of its nature the $13,000 expenditure does not qualify for depreciation. In this latter regard, it is claimed that depreciation of an intangible asset is only allowed when the asset in question

is limited in its useful life and its partial exhaustion can be computed with reasonable accuracy, citing Shufflebarger v. Commission, 24 T.C. 980 (1955). Treas. Reg. § 1.167 (a)-3. We generally agree with the Government's position.

It is well established that the statute authorizing a deduction from gross income of all ordinary and necessary business expense does not authorize a deduction for capital expenditures. Welch v. Helvering, 290 U.S. 111 (1933). In distinguishing the two, in United States v. Akin, 248 F. 2d 742 (10th Cir. 1957), cert. denied, 355 U.S. 956 (1957), appears the following pertinent comment:

> "* * * It is not always easy to find a verbal formula which readily supplies an unerring guide in drawing the boundary line between current expenses and capital outlays. But it may be said in general terms that an expenditure should be treated as one in the nature of a capital outlay if it brings about the acquisition of an asset having a period of useful life in excess of one year or if it secures a like advantage to the taxpayer which has life of more than one year * * *."

An analogous case quite helpful in resolving the present controversy is Nachman v. Commissioner of Internal Revenue, 191 F.2d 934 (5th Cir. 1951). We subscribe to its rationale and accordingly will refer to it at length.

In **Nachman**, the taxpayer purchased an existing municipal retail liquor license for the sum of $8,000. The li-

cense in question was an annual one issued by the municipality for a fee of $750, and when purchased by the taxpayer had some five months to run before it expired. The licenses were assignable and carried with them valuable renewal privileges, "as it was the established practice in issuing renewal licenses from year to year to prefer the holders of existing licenses over other applicants." The taxpayer then sought to deduct from his gross income as an ordinary and necessary business expense the entire $8,000 paid for the license. The Tax Court held that the taxpayer was entitled to deduct as an ordinary business expense the $750 license fee, but was not entitled to deduct the balance of the sum paid for the license, namely $7,250. In upholding this determination by the Tax Court the following comment was made which is repeated here because of its peculiar applicability to the present controversy:

> "Of course it was necessary for petitioners to have a license before they could commence business. None could be procured directly from the City, as the maximum number allowed by law had already been issued. Like other scare commodities, they commanded a premium on a seller's market. The license carried with it by established custom, if not by law, a valuable renewal privilege indispensable to petitioners' continuance in business in subsequent years. In purchasing the license, petitioners bought not only the operating right for the current year but also renewal privileges for future years. This privilege, entitling petitioners

to preference over non-license holders in the issuance of renewal licenses, was of substantial value, of which the seller and the purchasers of this license were well aware. No one would pay $8,000 for a $750 license having only five months to run, unless the purchaser was reasonably sure it carried with it appurtenant privileges of substantial future value to the purchaser. It was these considerations that prompted petitioners to pay $8,000 for a $750 license, of which only 5/12ths remained.

"Of the $8,000 paid for the license in question, the official cost of issuance, $750, was an ordinary and necessary business expense. The remaining $7,250 was the expenditure of capital in the acquisition of a capital asset reasonably expected to serve petitioners through future years, the cost of which is not deductible as an ordinary expense. * * *

"Petitioners further contend that if the $7,250 in question be regarded as the purchase price of a capital asset and therefore not deductible as ordinary business expense, they are entitled to an amortized depreciation allowance on such capital asset under 26 U.S.C.A. § 23, and Treasurey Regulation No. 111, sec. 29.23(1)-3, relating to depreciation of intangible property. Depreciation allowance on intangibles, however, is confined to those definitely limited in duration, such as patents, franchises, copyrights, licenses for fixed periods, and the like, the partial exhaustion of which may be computed with reasonable certainty.

"It is clear that the renewal privilege appurtenant to this license extends beyond, and was actually exercised beyond, the taxable year in question. Presumably the petitioners may continue to exercise their renewal privileges as long as they desire, as there is no indication that the City will depart from its custom of renewing existing licens-

es. How long petitioners may wish to continue exercising their renewal privileges is indeterminable. It might be for one year, or many. It was exercised by them at least as late as 1949. The basis for depreciation of an intangible capital asset is partial exhaustion due to lapse of time. This renewal privilege being of indefinite duration, dependent upon petitioners' wishes as well as upon the City's future course of action, there is no rational basis for prediction as to duration.

"Moreover, if petitioners elect to discontinue the exercise of their renewal rights, it is reasonable to assume that they will sell them, just as did their predecessor Bryan, either recouping their investment or sustaining a deductible loss. We conclude therefore, as did the Tax Court, that the renewal privilege incident to the license is a nondepreciable capital asset. * * *."

To like effect, see such cases as Richmond Television Corp. v. United States, 354 F.2d 410 (4th Cir. 1965); Commissioner v. Indiana Broadcasting Corp., 350 F.2d 580 (7th Cir. 1965), **cert. denied**, 382 U.S. 1021 (1966); and KWTX Broadcasting Co. v. Commissioner, 272 F.2d 406 (5th Cir. 1959), 31 T.C. 952 (1959), **aff'd per curiam**, involving the acquisition of television and radio licenses.

It is for these reasons that we hold that the trial court erred first in its finding that there was no reasonable certainty that the Land Office would renew the lease which the taxpayers had acquired from the Neiman estate and then erred further in concluding that the $13,000 paid for the lease was deductible from taxpayers' gross income as

an ordinary and necessary rental expense incurred in taxpayers' farm operations for the 1966 tax year.

Judgment reversed and the case is remanded with directions that the trial court enter judgments in favor of the Government.

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

CONSOLIDATED CASES

Civil No. 71-10

Norman and Virginia Shutler,

Plaintiffs,

v.

United States of America,

Defendant.

Civil No. 71-11

A. H. and Edith Turner,

Plaintiffs,

v.

United States of America,

Defendant.

JOURNAL ENTRY OF JUDGMENT

On this 28th day of May, 1971, this cause having been submitted to the Court upon stipulated facts and upon briefs of counsel, and the Court having reviewed all of the evidence and the briefs of counsel finds, orders, adjudges and decrees that the complaint of plaintiffs be sustained.

The Court further finds: (a) That it properly has

jurisdiction over this cause. (b) That the complainants acquired a lease on certain lands in the State of Oklahoma under the jurisdiction of the Commissioners of the Land Office and paid therefor $13,000.00 attributable to the acquisition of said lease, which sum was paid during the year, 1966, for a lease which expired December 31, 1966. (c) That said lease contained no options, and there was no reasonable certainty that the Commissioners of the Land Office would renew said lease for any given period of time. (d) That the Administration of said leases is subject to the whims of the Oklahoma Legislature, which meets every year and which has over the years enacted and repealed various laws dealing with the Administration of State lands.

Wherefore, it is the order and judgment of this Court that the plaintiffs, A. H. Turner and Edith Turner, recover from the defendant the sum of $1,151.73, together with the proper amount of interest at six percent to the date paid, and the plaintiffs, Norman Shutler and Virginia Shutler, recover from the defendant the sum of $4,397.25, together with the proper amount of interest at six percent to the date paid.

s/Stephen S. Chandler
United States District Court Judge

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

No. 71-10

NORMAN SHUTLER and

VIRGINIA SHUTLER,

Plaintiffs

v.

UNITED STATES OF AMERICA,

Defendant

No. 71-11

A. H. TURNER and

EDITH TURNER, Plaintiffs

v.

UNITED STATES OF AMERICA,

Defendant

AMENDMENT TO JOURNAL ENTRY OF JUDGMENT

It having been brought to the attention of this Court that the amounts to be recovered by the respective plaintiffs, as set forth in the Journal Entry of Judgment entered herein on May 28, 1971, are erroneous, and it further appearing that the parties have agreed upon the correct amounts to be recovered by the respective plaintiffs, pur-

suant to this Court's decision in these cases, it is hereby,

ORDERED, ADJUDGED, and DECREED that the Journal Entry of Judgment entered in these cases on May 28, 1971, should be, and is hereby, amended to delete the respective amounts of recovery awarded plaintiffs therein, and to substitute instead the following:

It is the order and judgment of this Court that plaintiffs, A. H. Turner and Edith Turner, have and recover from the defendant the sum of $1,046.45, plus interest as allowed by law, and that plaintiffs, Norman and Virginia Shutler, have and recover from the defendant the sum of $5,180.50, plus interest as allowed by law.

s/Stephen S. Chandler
United States District Judge

APPROVED AS TO FORM:
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s/Thomas E. Baker
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ATTORNEY FOR PLAINTIFFS
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s/Eugene G. Sayre
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Dallas, Texas 75202

ATTORNEY FOR DEFENDANT

(Judgment entered in Civil Docket on July 8, 1971. Adelaide Holston, Deputy.)

JANUARY TERM — JANUARY 22, 1973

Before Honorable David T. Lewis, Chief Judge, Honorable William J. Holloway, Jr., and Honorable Robert H. McWilliams, Circuit Judges

No. 71-1496

NORMAN SHUTLER and
VIRGINIA SHUTLER,
Plaintiffs-Appellees,

v.

UNITED STATES OF AMERICA,

Defendant-Appellant,

A. H. TURNER and

EDITH TURNER,

Plaintiffs-Appellees,

v.

UNITED STATES OF AMERICA,

Defendant-Appellant.

This matter comes on for consideration of the petition for rehearing filed by the appellees.

Upon consideration whereof, the petition for rehearing is denied.

In the Supreme Court of the United States

OCTOBER TERM, 1972

No. 72-1308

NORMAN SHUTLER AND VIRGINIA SHUTLER;
A. H. TURNER AND EDITH TURNER, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioners claim that they are entitled to deduct from their gross income for the year 1966 amounts expended in acquiring a leasehold in a quarter section of agricultural or grazing land owned by the State of Oklahoma. The record in this case, based upon fully stipulated facts, does not support petitioners' claim. The decision below is correct. There is no conflict of decisions or any other ground for further review.

Petitioners, co-tenants in farming operations in Oklahoma, purchased at an estate auction a leasehold in agricultural or grazing land owned by the State of Oklahoma and supervised by the Oklahoma State Land Office. They paid for the lease a total of $15,000, of which $13,000 was allocated to the cost of acquiring the lease and $2,000 to improvements.

The annual rent, set by the Land Office, was $850. Upon petitioners' purchasing the lease, the estate, pursuant to the requirements of the Land Office, executed a relinquishment in favor of the petitioners, who thereafter made formal application for and obtained the lease for its remaining period of less than five months, and subsequently for an additional lease period. (Pet. App. 11-13.)

The Oklahoma State Land Office enters into many agricultural and grazing leases, all of which run concurrently for five-year periods. Under those designated "preference right leases," such as the one in the instant case, the state contractually grants the lessee the preferential right to purchase the land for an amount equal to the highest bid, if and when the land is sold. However, in practice these lands have almost never been sold; instead, the lessee is given the right to re-lease the land indefinitely upon expiration of each lease period. (Pet. App. 13.)

Section 162 of the Internal Revenue Code of 1954 allows a taxpayer to deduct from gross income all the ordinary and necessary business expenses incurred in carrying on his trade or business during the taxable year. This Court's decisions have established that the ordinary and necessary business expense deduction does not include capital expenditures (*Welch* v. *Helvering*, 290 U.S. 111), and that an expenditure that results in the acquisition of an asset having a useful life of more than one year, such as a leasehold for a term longer than a year, should be treated as a capital expenditure (*Commissioner* v. *Lincoln Savings & Loan Assn.*, 403 U.S. 345, 352, 354; *United States* v. *Catto*, 384 U.S. 102, 109; *Deputy* v. *duPont*, 308 U.S. 488). Furthermore, although the cost of a lease

may often be amortized over its term (Treasury Regulations on Income Tax (1954 Code) §1.162-11, cited by taxpayer, Pet. 5), when that term can be determined with reasonable certainty (Section 178 (c), Internal Revenue Code of 1954), a lease or other asset which is reasonably certain to be renewable for an indefinite period may not be amortized. *Nachman* v. *Commissioner,* 191 F. 2d 934 (C.A. 5); *KWTX Broadcasting Co.* v. *Commissioner,* 272 F. 2d 406 (C.A. 5); *Commissioner* v. *Indiana Broadcasting Corp.,* 350 F. 2d 580 (C.A. 7); and *Richmond Television Corp.* v. *United States,* 354 F. 2d 410 (C.A. 4).

Here the court of appeals, on the basis of the stipulated Rules and Regulations of the Commissioners of the Land Office, concluded that it was the policy and the unvarying practice of that office, carried out in this case, to renew indefinitely these five-year leases of agricultural and grazing lands. Accordingly, the court held that petitioners were not entitled to deduct the cost of acquiring the lease in the year of acquisition.[1] The court's holding with respect to that factual determination does not require further review.[2]

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[1]Indeed, though the point was not directly in issue, the court's holding would also preclude petitioners from amortizing the cost of acquiring the leasehold over the original period plus the first five-year renewal period, on the ground that petitioners could, and were likely to, continue to renew the lease indefinitely.

[2]Petitioners' reliance upon *Scully* v. *United States,* 409 F. 2d 1061 (C.A. 10), is misplaced, since that case turns on technical principles used in condemnation suits to determine the value of a leasehold interest, rather than on the principles applied under federal tax statutes to determine whether an expenditure is for the acquisition of a capital asset.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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